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Consultation response

EBA Consultation on draft Guidelines on Liquidity Coverage Ratio ('LCR') Disclosure

27 July 2016

The Association for Financial Markets in Europe (AFME) welcomes the opportunity to comment on the European Banking Authority's (EBA's) consultation on draft Guidelines on Liquidity Coverage Ratio ('LCR') Disclosure. AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society.

AFME is the European member of the Global Financial Markets Association (GFMA) a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) in Asia.

AFME is listed on the EU Register of Interest Representatives, registration number 65110063986-76.

We summarise below our high-level response to the consultation, which is followed by answers to the individual questions raised.

Overview/Executive Summary

AFME and its members support strongly the principle of disclosure by firms of information and data in relation to the LCR to enhance market understanding of banks' liquidity risk profile. We consider, however, that the requirements as currently drafted would be too granular to be effective for users and could prove counterproductive.

In general we would agree with the scope of the application of the disclosure requirements but it will be important to ensure that sufficient flexibility is maintained so that the level of disclosure remains meaningful. There is also a lack of clarity surrounding the application date of the disclosure requirements, which in our view should not commence until the requirement for firms to meet 100% of their LCR comes into effect from January 2018.

In the meantime, we have set out observations where the proposed requirements diverge from the BCBS standard and it will be important to mitigate the risk that sensitive information which is prepared for risk management and regulatory purposes might need to be disclosed.

We have noted also that we consider that LCR disclosure should be based on six month rolling average values of monthly observations.

Question 1:

AFME and its members note that the scope of the application of the guidelines is limited to credit institutions subject to disclosure requirements under the CRR and at the same level as envisaged in the LCR Delegated Act. We welcome therefore that firms which have been waived from the LCR requirement on a solo basis would not fall in the scope of the individual disclosure of the LCR. There may, however, be instances where liquidity risk management arrangements apply from higher levels within a group or sub-group and the disclosure of qualitative information on these arrangements may therefore be more appropriate at such levels. In all cases, there would be no advantage to disclosure in

relation to large numbers of individual entities which would overwhelm the user with large volumes of data and present distorted views of groups' risk profile.

Furthermore, CRR Article 6(3) states that an institution which is part of a consolidated group which is subject to Part Eight of the CRR does not need to comply with Part Eight on an individual basis.

Question 2:

We would welcome further clarification on the application date for disclosure and we suggest that disclosure should not apply until firms are required to meet 100% of their LCR calculation from January 2018.

At present, it is not clear whether firms would be expected to disclose information on the LCR from June 2017 or whether this might be the date from which the guidelines apply with disclosure envisaged from a later date. We would note in addition that in June 2017, under the LCR transitional arrangements firms will be required to meet only 90% of their LCR requirements and that it would be clearer for users therefore if disclosure was to commence from 2018 when firms will have to meet their LCR requirements in entirety.

There will also need to be adequate mechanisms in place to ensure that changes expected under the LCR corrigendum are considered in sufficient time to avoid requiring firms to prepare disclosures in accordance with differing standards.

Question 5:

We note that Annex 1 appears to request the submission of qualitative information in a tabular format. It is questionable though whether this will deliver much value as firms already publish this type of information more fully as part of their Pillar 3 disclosure.

This qualitative disclosure template departs significantly from the Basel Pillar 3 Disclosure requirements with regards to the type of information required, the level of granularity and, unlike the Basel approach, does not allow firms the flexibility to choose the relevant information to disclose. The EBA should align with the Basel approach and allow respondents to provide their own qualitative inputs which will vary depending on their business model and degree of liquidity and funding risks to which they are exposed. Requiring EU banks to provide additional, potentially highly sensitive material could distort the global level playing field and exacerbate any market confidence issues affecting credit institutions or create new vulnerabilities that can be exploited in stressed markets. By providing the market with relatively specific information about an institutions liquidity risk profile, risk tolerance limits and business strategy could inhibit the institutions ability to execute those strategies. For example, market participants could anticipate an institution's planned liquidity actions, thereby facilitating anti-competitive or "front-running" behaviour and constraining and institutions ability to respond to certain conditions. We would continue to note also that requiring the disclosure of information at too granular a level or requiring a declaration from management is likely to over-burden users and firms and that it could prove counterproductive.

In addition we note that elements of the qualitative requirements are very similar to what is required by the European Central Bank as part of the ICAAP and ILAAP submission process. Such statements contain sensitive information for regulatory purposes which is not suitable for disclosure to market participants.

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Question 6:

As mentioned, we question if the level of granularity proposed for the LCR disclosure template would be useful to market participants and therefore achieve the transparency objective of such disclosures. Disclosure of granular information on possibly volatile figures might increase the risk of misunderstandings by market participants. Such a situation would be counterproductive compared to be fundamental intentions behind the disclosure requirements. In our opinion, if such detailed granularity is required, it may lead to information overload for investors and could exacerbate a liquidity stress scenario if market participants were to misinterpret the data.

Question 7:

We would note that it is not clear what is being requested in relation to 'Derivatives exposures and potential collateral calls' and that 'a description of the degree of centralisation of liquidity management' would have been provided already in Annex 1.

Further clarity is needed regarding the disclosure requirement of other inflows and outflows that are not captured in the LCR common template. If the disclosure requirement is not specifically defined, there may be unintended consequences regarding the disclosure of sensitive regulatory or proprietary information that is not suitable for market participants and which may lead to inconsistencies in disclosures between institutions.

Separately, regulators have still to decide upon and define LCR requirements in relation to material currencies and it would appear anomalous for firms to be disclosing information before a regulatory standard has been agreed.

In addition, if banks are expected to disclosure the 'currency mismatch in the LCR', it is important the means for calculating the ratio by material currency is clearly defined on a common basis. There appears to be some inconsistency in the way the Delegated Act on the LCR, and EBA ITS on LCR reporting, have interpreted the treatment of maturing foreign currency derivatives in the LCR. Delegated Act Article 21 allows FX transactions to be treated on a net basis: *"Cash outflows and inflows arising from foreign currency derivative transactions that involve a full exchange of principal amounts on a simultaneous basis (or within the same day) shall be calculated on a net basis".*

The EBA ITS on reporting, on the other hand, requires banks to calculate the LCR ratio using foreign currency derivatives on a gross basis: *Netting by counterparty may only be applied to flows in that currency, for instance Counterparty A: EUR+10 and Counterparty A: EUR-20 shall be reported as EUR10 outflow. No netting shall be made across counterparties, for instance Counterparty A: EUR- 10, Counterparty B: EUR+40 shall be reported as EUR10 outflow on C73.00 (and EUR40 inflow on C74.00).*

LCR by Currency calculations in accordance with the ITS will lead to extreme outcomes, rendering the ratio unusable for internal risk management, supervision, or external disclosure.

Question 8:

As stated above in our response to Question 6, we question if the level of granularity proposed would be more relevant or meaningful to investors when compared to a simplified disclosure based only on the ratio itself and the numerator and the denominator. We understand that more detailed information is required by legislation for supervisory purposes but the requirements for market participants are quite different. Therefore we would question the value that public disclosure of line items 19 a, 19b, 20a, 20b and 20c would give outside market participants. As stated above, the disclosure of such granular information provides little intrinsic value and could increase the risk of misunderstandings. Such an outcome is in contrast with the original objective of such disclosure requirements.

In addition, these items are more granular than proposed by Basel during the recent Pillar 3 consultation exercise and we would question how the public release of such granular information would achieve the objective of providing market participants with relevant information on the liquidity positions of credit institutions. In the interests of maintaining a global level playing field we reiterate our belief that the LCR disclosure templates should be aligned with the BCBS Pillar 3 requirements.

Question 11:

AFME and its members would suggest that the LCR disclosure template should be based on a six month rolling average of monthly LCR observations, to be reported on a quarterly basis. Given that supervisory reporting is monthly in the EU[1], it appears unwarranted to prescribe a higher calculation frequency for public disclosure purposes. The additional calculations needed to allow averaged values over daily observations would therefore be operationally complex and burdensome with no clear value for the end user.

Further Observations

In addition to our thoughts on the specific questions raised, we would note also our assumption that national competent authorities will not require the disclosure of LCR information until the EBA guidelines are adopted.

From a practical perspective, it would be useful for the industry if the EBA was able to prepare a validation spreadsheet that maps the relevant supervisory reporting forms to the LCR disclosure template.

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[1] See Commission Implementing Regulation (EU) no. 680/2014